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Choateness and the 1966 Federal Tax Lien Act

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I. INTRODUCTION

The Federal Tax Lien Act provides that, immediately upon the assessment[1] of a tax deficiency, a lien attaches to all property of the delinquent taxpayer.[2] Because a delinquency in the payment of taxes is often caused by a general deterioration of the taxpayer's financial position, a failure to pay the tax is generally accompanied by an inability to pay other outstanding debts including those owing to private creditors. Accordingly, imposition of the federal tax lien generally results in a conflict between the tax claim of the federal government and private creditors' claims. This conflict becomes significant if the total property of the taxpayer is not sufficient to satisfy all the competing claims. Prior to 1966 the provisions of the Internal Revenue Code did not establish a priority among these competing interests. Yet, decisions of the United States Supreme Court, through application of a "choateness" doctrine, greatly favored the tax lien over the competing interests,[3] causing an undermining of the security of many common financial transactions.

The 1966 Federal Tax Lien Act represents an attempt to attain a more reasonable accommodation between the interests of the federal government in the collection of delinquent taxes and the needs of the business community in assuring the proper functioning of the private credit system.[4] It is also intended to correlate the tax lien provisions with the many changes in commercial law, most notably the wide acceptance of the Uniform Commercial Code, which occurred since the last comprehensive revision of the tax lien statute.[5]

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1. The act of assessment is an administrative procedure which is performed by the Internal Revenue Service. No public notice of assessment is given, and the procedure is not open to public inspection.

2. INT. REV. CODE of 1954, § 6321.

3. There has been extensive writing on the topic of tax lien priority. *See, e.g.*, Kennedy, *From Spokane County to Vermont: The Campaign of the Federal Government Against the Inchoate Lien*, 50 IOWA L. REV. 724 (1965); Kennedy, *The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien*, 63 YALE L.J. 905 (1954); Plumb, *Federal Tax Collection and Lien Problems*, 13 TAX L. REV. 459 (1958); Wolfson, *Federal Tax Liens—A Study in Confusion and Confiscation*, 43 MARQ. L. REV. 180 (1959); Note, 43 MINN. L. REV. 755 (1959).

4. *Hearings on H.R. 11256 and H.R. 11290 Before the Committee on Ways and Means of the House of Representatives*, 89th Cong., 2d Sess. 5, 41 (1966).

5. *Hearings on H.R. 11256 and H.R. 11290, supra* note 4, at 37.

The function of this Note is to review the development and effects of the choateness doctrine under the prior federal tax lien provisions. Thereafter, the extent to which the 1966 Federal Tax Lien Act was intended to limit the choateness doctrine will be examined, and the consequences of this limitation will be evaluated.

II. JUDICIAL DETERMINATION OF RELATIVE PRIORITIES UNDER THE FORMER TAX LIEN ACT

The common law rule for determining priority between competing creditors, "first in time, first in right,"[6] was judicially applied to the determination of the priority of interests competing with tax liens of the federal government.[7] Since the tax lien attaches at the time of assessment of the tax deficiency, only those interests created prior to the assessment prevailed under this rule.

However, because tax assessments were not made public, a creditor could in good faith enter a financial agreement with a delinquent taxpayer unaware that his interest was already subordinate to a secret tax lien. The inequities of this secret lien resulted in congressional adoption of the notice-filing provision,[8] which gave priority to mortgagees, pledgees, purchasers, and judgment creditors whose interests were created prior to the filing of the tax lien.[9] The priorities of all other interests were fixed, as before, according to the date of the tax deficiency assessment.

A. Evolution and Application of the Choateness Doctrine

As originally developed under the federal priority statute,[10]

6. Rankin v. Scott, 25 U.S. (12 Wheat.) 177, 179 (1827).

7. *See, e.g.*, United States v. Pioneer Am. Ins. Co., 374 U.S. 84 (1963); United States v. City of New Britain, 347 U.S. 81 (1953).

8. For the historical development of the notice-filing provision, see Kennedy, *The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien*, 63 YALE L.J. 905, 920-22 (1954).

9. 68A Stat. 779 (1954). This section was originally enacted to remedy the harsh rule of United States v. Snyder, 149 U.S. 210 (1893), which allowed secret tax liens to gain priority over purchasers and mortgagees acquiring their interest between the attaching and the filing of the lien. *See* United States v. Union Cent. Life Ins. Co., 368 U.S. 291, 294-95 (1961).

10. *See* County of Spokane v. United States, 279 U.S. 80 (1929). *See generally* Kennedy, *From Spokane County to Vermont: The Campaign of the Federal Government Against the Inchoate Lien*, 50 IOWA L. REV. 724 (1965).

the doctrine of choateness required the identity of the lienor,[11] the amount of the lien,[12] and the property subject to the lien[13] to be known and definite before the competing interest was deemed choate.

The time at which the interest became choate, rather than the time the interest attached, determined priority. *United States v. Security Trust*[14] held the choateness doctrine determinative of the relative rights of competing interests under the tax lien act. The Court in *United States v. City of New Britain*[15] explicitly articulated the three requisites of choateness as applicable to statutory liens competing with the federal tax lien.

The several per curiam decisions of the Court subsequent to *New Britain*, which denied priority to statutory mechanic's liens, illustrate the application of the choateness doctrine.[16] It was held that unless the mechanic's lienor obtained a judgment prior to the attachment of the tax lien his interest was inchoate and inferior.[17] Apparently the rationale was that the lien was merely an interim step toward the status of a judgment creditor and until the mechanic's lienor became a judgment creditor the amount of the lien remained uncertain.[18] However, in *United States v. Vermont*,[19] the Court held that a state tax lien was

11. *See* United States v. Knott, 298 U.S. 544 (1936).

12. *See* United States v. Waddill, Holland & Flinn, Inc., 323 U.S. 353 (1945); United States v. Texas, 314 U.S. 480 (1941).

13. *See* Illinois *ex rel.* Gordon v. Campbell, 329 U.S. 362 (1946); United States v. Waddill, Holland & Flinn, Inc., *supra* note 12.

14. 340 U.S. 47 (1950). In *Security Trust* the Court held that the amount of a local statutory lien, which had attached but had not been reduced to judgment before the tax lien arose, was uncertain and thus inchoate and junior to the federal tax lien. The effect of this decision was to overrule at least thirty cases which had applied the federal tax lien statute literally, giving priority to the interest which first attached. *See* Kennedy, *supra* note 8, at 924 n.115.

15. 347 U.S. 81 (1954).

16. *See, e.g.*, United States v. Hulley, 358 U.S. 66, *reversing* 102 So. 2d 599 (Fla. 1958); United States v. Vorreiter, 355 U.S. 15, *reversing* 134 Colo. 543, 307 P.2d 475 (1957); United States v. White Bear Brewing Co., 350 U.S. 1010 (1956), *reversing* 227 F.2d 359 (7th Cir. 1955); United States v. Colotta, 350 U.S. 808, *reversing* 224 Miss. 33, 79 So. 2d 474 (1955). *See generally* Note, 63 YALE L.J. 138 (1958).

17. United States v. White Bear Brewing Co., *supra* note 16.

18. Although the per curiam decisions did not articulate a rationale, it has been suggested that the amount of the mechanic's lien cannot be determined until all possible defenses to the lien have been settled by judicial decision. United States v. Bond, 279 F.2d 837, 849 (4th Cir. 1960).

19. 377 U.S. 351 (1964), *affirming* 317 F.2d 446 (2d Cir. 1963).

sufficiently choate to prevail against the federal lien even though it had not been reduced to judgment. However, because the Vermont statutory lien itself had the force of a judgment,[20] the *Vermont* decision probably will not support an argument that a statutory lien need no longer to be reduced to judgment to prevail against the federal tax lien.

The Supreme Court, by per curiam decisions,[21] also extended the applicability of the choateness doctrine to consensual liens included within the notice-filing provision. For example, in *United States v. Ball Construction Co.*,[22] a security agreement was entered into prior to the attachment of the tax lien whereby present or future funds due to a contractor were assigned to a surety as security for its promise to guarantee the contractor's performance. The lien was deemed inchoate and inferior to the federal tax lien, apparently on the ground that because the surety might be required to make payments after the tax lien was filed the amount of the lien was uncertain.[23]

In *Crest Finance Co. v. United States*,[24] a subcontractor assigned amounts due from the general contractor as security for loans made to the subcontractor. A tax lien attached to the property of the subcontractor at a time when the work under

20. The Court, in the *Vermont* decision, stated that "the assessment is given the force of a judgment, and if the amount assessed is not paid when due, administrative officials may seize the debtor's property to satisfy the debt." 377 U.S. 351, 358-59 (1964). *See generally* Weir, *Competition Among Federal and California Tax Liens and Creditor's Liens*, 17 U. So. CAL. 1965 TAX INST. 807.

21. Crest Fin. Co. v. United States, 368 U.S. 347 (1961), *vacating* 291 F.2d 1 (7th Cir. 1961); United States v. Ball Constr. Co., 355 U.S. 587 (1958), *reversing* 239 F.2d 384 (5th Cir. 1957), *affirming* 140 F. Supp. 60 (W.D. Tex. 1956).

22. 355 U.S. 587 (1958).

23. The per curiam decision in *Ball* merely stated that the competing interest was inchoate. However, United States v. Pioneer Am. Ins. Co., 374 U.S. 84, 91 (1963), explained that the amount of the surety's lien in *Ball* was uncertain, and hence inchoate, at the time the federal tax lien was filed because the surety's obligation was contingent.

Pioneer also indicated that the security interest in *Ball* was deemed to be a "mortgage" within the notice-filing provision. If this is so and the mortgage was signed prior to the time the tax lien was filed, the policy of the notice-filing provision would seem to indicate that the secured party in *Ball* should have been given priority. However, the Court in *Pioneer* stated:

> [W]e believe Congress intended that if out of the whole spectrum of state-created liens, certain liens are to enjoy the preferred status granted by [the notice-filing section], they should at least have attained the degree of perfection required of other liens and be choate for the purposes of the federal rule.

374 U.S. at 89.

24. 368 U.S. 347 (1961).

the subcontract had been completed but the exact amount due the subcontractor required ascertainment by engineering measurement. The court of appeals[25] held, on the authority of *Ball*, that the assignee's interest was inchoate because the amount due the subcontractor was uncertain. On appeal to the Supreme Court, the Solicitor General conceded that the *Ball* decision did not compel a finding of inchoateness. Accordingly, the Supreme Court vacated the judgment. The contrary findings of choateness in *Ball* and *Crest* may be explained by the fact that in *Ball* the future contingent disbursements could not be determined at the time of tax lien filing, whereas in *Crest*, because all obligations had been completed, the obligation of the contractor to the subcontractor was fixed and the amount payable to the subcontractor could have been calculated at the critical time.[26]

Thus, under prior law, statutory liens such as attachment and mechanic's liens obtained priority only if reduced to judgment when the tax lien attached. Contractual liens such as secured claims of mortgagees had priority only if the performance of the secured party were complete and the amount of the lien were fixed and definitely ascertainable at the time of assessment. However, if the contractual interest were included within the notice-filing provision it would take priority if choate at the time the tax lien was filed.

B. Effects of the Choateness Doctrine

The effect of the choateness doctrine was to subordinate certain statutory and contractual security interests without affording affected creditors a practical opportunity to protect themselves. Because the competition arises only when the debtor-taxpayer is insolvent, subordination of the private creditor often placed the risk of insolvency on the party least able to bear the risk of loss. Often the advancement made by creditors enhanced the value of the taxpayer's property and thus the choateness doctrine permitted the tax lien to appropriate, without compensation, value for which the creditor was responsible. The result

25. 291 F.2d 1 (7th Cir. 1961).

26. It has been contended that the best explanation of *Crest* is that the Solicitor General conceded choatness. *See* Kennedy, *supra* note 10, at 740.

However, in United States v. Pioneer Am. Ins. Co., 374 U.S. 84, at 91 n.9 (1963), the Court contrasted *Ball* and *Crest*, nothing that in *Crest* the assignment and the loans were consummated prior to the accrual and filing of the federal tax lien.

was an undermining of security interests in competition with the federal tax lien.[27]

Additional confusion was created by the conflicting priority systems of state and federal law. Most states grant priorities to certain creditors such as mechanics, materialmen, and local taxing authorities. However, the choateness doctrine often denied priority to these same interests. For example, state law may give a mechanic's lien preference over a pre-existing mortgage. If a federal tax lien were filed after a mortgage had become choate but before a mechanic's lien on the same property had been reduced to judgment, federal law regarded the federal tax lien as superior to the mechanic's lien but junior to the mortgage. Under state law, however, the mechanic's lien had priority over the mortgage. If there were insufficient proceeds to satisfy all the competing liens, a circuity problem resulted.[28]

Faced with such a circuity of lien rights problem, the Court in *United States v. City of New Britain*[29] evolved a two step analysis to resolve the dilemma. Under this approach, the federal law of priorities was applied first, and an amount equal to the interests that take priority over the federal tax lien was set aside to satisfy those interests. Thereafter, the federal tax lien and the remaining subordinate liens were satisfied in that order. If the value of the security was not sufficient to satisfy all the claims, the amount set aside to satisfy claims superior to the federal tax lien was allocated among the competing interests in order of the priority as determined by state law. Thus, in the example given, an amount sufficient to satisfy the mortgage would be allocated subject to redistribution under state law to

27. The harsh effects of the choateness doctrine were somewhat mitigated by judicial adoption of what has been termed the "no property" rule. Since the federal tax lien attaches only to property or property rights of the delinquent taxpayer, the tax lien may be limited or defeated to the extent that under state law the taxpayer has no property. *See, e.g.*, Aquilino v. United States, 363 U.S. 509 (1960); United States v. Durham Lumber Co., 363 U.S. 522 (1960).

For example, in *Aquilino*, the federal government had assessed a tax deficiency against a general contractor and had thereby perfected its lien against proceeds of the construction contract. However, because state law made the payments received by a contractor a trust fund for the benefit of unpaid subcontractors, and because the subcontractors remained unpaid, the contractor was deemed to have no property upon which the federal lien could attach, until all subcontractors were paid. *See generally* Kennedy, *supra* note 10, at 752; Comment, 24 MD. L. REV. 310 (1964).

28. *See generally* Oppenheim, *Federal Tax Liens: Evolution and Conflict With State Liens*, 4 DUQUESNE U.L. REV. 494, 510 (1965-1966).

29. 347 U.S. 81 (1954).

satisfy the mechanic's lien. The bizarreness of this approach is exemplified by the fact that, in the situation given, the mechanic's lien is saved because of the mortgage which was junior to it under state law. Furthermore, the mortgage may receive none of the security whereas the purportedly junior federal tax lien received partial or complete satisfaction.[30]

III. CONGRESSIONAL LIMITATION OF THE CHOATENESS DOCTRINE

Many years of cooperative work among the American Bar Association, the Treasury Department, and the staff of the Joint Committee on Internal Revenue Taxation culminated in passage of the 1966 Federal Tax Lien Act. One of the major objectives of the new act was to reform the choateness doctrine and thereby eliminate or minimize the inequities and impediments to business transactions which it created.[31] Although the choateness doctrine was to be reformed, the legislative history indicates that it was not to be completely eliminated.[32] However, the extent to which the doctrine remains is not made clear by the 1966 Act. Indeed, the Act makes no express reference to the choateness doctrine, and the terminology of the Act cannot be deemed determinative of the question.[33] It is therefore necessary to examine the changes made by the new Act which are relevant to the choateness doctrine, and thereby determine the extent to which Congress intended to limit the doctrine.

In attempting to make the rules governing tax liens more equitable and certain under the 1966 Act, Congress strengthened the rights of private creditors competing with the tax lien.[34] This is primarily accomplished by three basic changes. Section 6323(b) of the 1966 Act specifies ten interests that are afforded a "superpriority" status. Section 6323(c) and (d) specify that security interests arising under certain commercial financing agreements are given priority over the tax lien even if they at-

30. This attempt to resolve the circuity of lien rights problem also frustrates the judicial policy against permitting inchoate interests to prevail against the tax lien, for the effect may be to satisfy inchoate interests first.

31. *Hearings on H.R. 11256 and H.R. 11290, supra* note 4, at 64.

32. *Id.* at 45, 47.

33. Although §§ 6323(a), (b), (c), and (d) of the 1966 Federal Tax Lien Act state that the federal lien "shall not be valid" against certain interests, decisions under the former act construed the same phrase to provide that such interests would prevail over the tax lien only if choate. *See, e.g.*, United States v. Ball Constr. Co., *supra* note 21.

34. 112 CONG. REC. 21,311 (daily ed. Sept. 12, 1966).

tach after the tax lien is filed. Finally, section 6323(a) broadens the classification of interests included within the notice-filing provision.

A. THE SUPERPRIORITY INTERESTS

Section 6323(b) of the 1966 Act defines certain limited interests that take priority over a federal tax lien even though they arise after the tax lien has attached and notice thereof has been filed.[35] These interests are deemed "superpriorities." Granting of superpriority status was thought to be justified by the nature of the interests protected.[36] Most of these interests involve casual and common transactions of relatively limited amount for which an individual cannot be expected to

35. INT. REV. CODE of 1954, § 6323(b) provides that, even though notice of the federal tax lien has been filed, it shall not be valid against:

(1) A purchaser of securities, such as bonds and debentures, or a holder of a security interest in such securities, provided that the purchaser or holder did not have knowledge of the tax lien when the interest arose. *See* § 6323(b)(1).

(2) A purchaser of a motor vehicle who did not have knowledge of the tax lien at the time of purchase or before he took possession of the vehicle, and who has not relinquished possession to the seller. *See* § 6323(b)(2).

(3) A purchaser in the ordinary course of business of tangible personal property at retail, provided that the purchaser has no intent to hinder or defeat the tax lien. *See* § 6323(b)(3).

(4) The purchaser of personal property such as household goods and personal effects purchased in a casual sale for less than $250, provided the purchaser does not have knowledge of either the tax lien or the fact that the sale is one of a series of sales. *See* § 6323(b)(4).

(5) A person with a possessory lien for repair or improvement on personal property who has maintained possession since the time of tax lien filing. *See* § 6323(b)(5).

(6) State and local real property and special assessment tax liens which, under local law, are entitled to priority over security interests that are prior in time. *See* § 6323(b)(6).

(7) Mechanic's lienors who have a lien for repair or improvement of a personal residence if the contract price does not exceed $1000. *See* § 6323(b)(7).

(8) An attorney who has a lien for reasonable fees on a judgment in favor of the delinquent taxpayer. *See* § 6323(b)(8).

(9) An insurance company that has, under certain qualifications, made loans to the insured-taxpayer on a life insurance, endowment, or annuity contract. *See* § 6323(b)(9).

(10) A bank or similar institution which has made loans to the taxpayer secured by a savings deposit or other account with that institution and evidenced by a passbook, provided that the loan was made without knowledge of the tax lien and provided further that the pass book has been continuously in the possession of the lending institution. *See* § 6323(b)(10).

36. *See Hearings on H.R. 11256 and H.R. 11290, supra* note 4, at 46-47.

check for filed tax liens prior to entering each transaction, while other superpriority interests tend to enrich the taxpayer's property.[37]

Because the superpriorities take priority over a tax lien even if they arise subsequent to assessment of the tax and filing of the lien, it seems clear that the choateness doctrine no longer applies to any of these interests.[38] This conclusion is supported by decisions holding that the two superpriorities under the prior act[39] could "take from a tax liened debtor with impunity from the lien."[40] It is the intention of the 1966 Act to continue this rule of impunity for superpriority interests.[41]

B. Interests Based on Commercial Financing Transactions

The choateness doctrine appears to be further limited by sections 6323(c) and (d) of the 1966 Act dealing with commercial financing agreements. Generally, such an agreement is entered into by the taxpayer and a third party obligating the third party to make future advances or obligatory payments upon the happening of a condition precedent. These disbursements are secured either by property existing at the time of the agreement, or property to be acquired thereafter. Sections 6323(c) and (d) of the 1966 Tax Lien Act define in detail four such commercial financing arrangements and grants them priority over the tax lien in certain circumstances.

The first[42] is an agreement between the taxpayer and a commercial financier whereby the financier agrees to make loans secured by "commercial financing security,"[43] or to purchase com-

37. *Compare* Uniform Commercial Code § 9-302, which specifies certain perferred security interests that will be perfected without filing.

38. A written statement by the Assistant Secretary of the Treasury explained certain of the proposed superpriorities under the topic of "Expansion of classes of property entitled to protection against a filed Federal tax lien to encompass interests which are not technically 'choate,' but which are related to an earlier, protected, security interest." *Hearings on H.R. 11256 and H.R. 11290, supra* note 4, at 38. *See* H.R. Rep. No. 1884, 89th Cong., 2d Sess. 4-7 (1966).

39. *See* 68A Stat. 779-80 (1954) (possessors of interests in bonds and securities); 78 Stat. 127 (1964) (purchasers of motor vehicles).

40. Worley v. United States, 340 F.2d 500, 501 (9th Cir. 1965). *See In re* Cle-Land Co., 157 F. Supp. 859 (D. Mass. 1958); United States v. Royce Shoe Co., 137 F. Supp. 786 (D.N.H. 1956).

41. *See Hearings on H.R. 11256 and H.R. 11290, supra* note 4, at 38; H.R. Rep. No. 1884, *supra* note 38, at 4.

42. *See* Int. Rev. Code of 1954, § 6323(c)(1), (2).

43. Commercial financing security is defined as "(i) paper of a kind ordinarily arising in commercial transactions, (ii) accounts re-

mercial financing security other than inventory. The secured party is given priority over the federal lien if the agreement was made before the tax lien was filed even though disbursement of payment is not made until after filing. The priority, however, is afforded only to disbursements or payments made within forty-five days after the filing of the tax lien and before the lender or purchaser acquires actual knowledge of the tax lien.[44] If the agreement so provides, the secured party will have priority as to property acquired by the debtor up to forty-five days after the tax lien is filed.[45]

Priority is similarly granted to a person who agrees to advance the taxpayer money to construct and improve real property, or to finance a contract to construct or improve real property, or to enable the taxpayer to raise or harvest farm crops or to raise livestock.[46] If such agreement is made prior to tax lien filing, the secured party has a priority over the tax lien as to property specified in the agreement, even though the disbursements are made after the tax lien filing.[47] Such priority is recognized because the advances of the secured party will usually enhance the value of the property of the taxpayer.[48]

Interests arising from an obligatory disbursements contract may also qualify for priority treatment.[49] Specifically, if prior to the filing of the tax lien, the taxpayer enters an agreement whereby a third party may be required to make disbursements because someone other than the taxpayer has relied on his obligation,[50] then the security interest of that third party in certain specified property[51] takes priority over the tax lien even

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ceivable, (iii) mortgages on real property, and (iv) inventory." INT. REV. CODE of 1954, § 6323(c)(2)(C).

44. INT. REV. CODE of 1954, § 6323(c)(2)(A).

45. INT. REV. CODE of 1954, § 6323(c)(2)(B). This provision permits the secured property to include after acquired property and it allows the financier to substitute new security for security being released.

46. INT. REV. CODE of 1954, § 6323(c)(1), (3).

47. The qualified property subject to the security interest will be either the real property constructed or improved, or the proceeds of the construction contract financed by the loan, or the crops and livestock financed by the loan. INT. REV. CODE of 1954, § 6323(c)(3)(B).

48. 112 CONG. REC. 21,293 (daily ed. Sept. 12, 1966).

49. *See* INT. REV. CODE of 1954, § 6323(c)(1), (4).

50. An example is an irrevocable letter of credit which the issuing bank must honor upon demand for payment by a third party who advances credit in reliance upon the letter. Similarly included are agreements by a surety to guarantee the performance of construction contracts.

51. The qualified property securing an obligatory disbursements

though the disbursements are made after the lien is filed. The secured party is protected because his obligation to make disbursements after the filing of the tax lien arises from an agreement made prior to filing[52] and, in the case of a suretyship contract, because the surety contributes to the creation of the asset by responding to the obligation and assuming the risk of contract performance.

In addition to these three commercial transaction financing agreements, section 6323(d) of the 1966 Act grants a more general priority to a person who, pursuant to an agreement entered prior to the lien filing, makes disbursements to the taxpayer without knowledge of the tax lien and within forty-five days after its filing.[53] The priority extends only to property existing at the time of the tax lien filing and specifically covered by the agreement.

The protection granted the secured party in the four above described situations is available only if the interest would be protected under local law against a judgment lien arising at the time of tax lien filing.[54] Since the Uniform Commercial Code

agreement must be property in existence at the time of tax lien filing or, if it comes into existence after that time, it must be directly traceable to the disbursement. INT. REV. CODE of 1954, § 6323(c)(4)(B). If the secured party is a surety company, qualified property also includes the proceeds of the contract the performance of which was ensured. INT. REV. CODE of 1954, § 6323(c)(4)(C).

Note, however, that if a taxpayer-contractor has a contract with the federal government, and if the surety guarantees either payment or performance of that contract, the qualified property subject to the claim of the surety may be greatly limited. In United States v. Munsey Trust Co., 332 U.S. 234 (1947), the Court held that the federal government may set off amounts due for taxes against amounts owed by it to the taxpayer under a contract. Nothing in the 1966 Act was intended to reverse the *Munsey* decision. *Hearings on H.R. 11256 and H.R. 11290 Before the Committee on Ways and Means of the House of Representatives*, 89th Cong., 2d Sess. 48 (1966).

52. 112 CONG. REC. 21,293 (daily ed. Sept. 12, 1966).

53. The forty-five day limitation represents a compromise between the interests of the secured party and the interests of the federal government. If no time limit existed, the taxpayer could, under the terms of a previously existing security agreement, convert all his property into spendable, concealable cash over an extended period of time. The act precludes such conversion after the forty-fifth day, and the Internal Revenue Service can shorten this period by giving notice to the secured party. On the other hand, if no time period were permitted, a secured lender would be required to check the records before each advance. The 1966 act requires him to do so only every forty-five days.

54. The Uniform Commercial Code generally requires filing of the interest as a requisite to such protection. UNIFORM COMMERCIAL CODE § 9-302. Arguably, filing is irrelevant in these situations because the federal government is not a reliance creditor and therefore does not

constitutes the local law in nearly every state, and as Congress intended to correlate the 1966 Federal Tax Lien Act with the concepts of the Uniform Commercial Code,[55] the Code will be assumed applicable where local law is relevant.

Under the Uniform Commercial Code, a secured party must perfect his security interest to be protected against competing creditors. Generally, a security interest is perfected when a financing statement has been filed and the interest has attached.[56] The security interest attaches when the secured party has given value and the debtor has rights in the collateral.[57] Therefore, if the secured party has filed, his security interest is perfected immediately upon making the first advance to the debtor.[58] For purposes of determining priority against a competing security interest or judgment lien, the perfected interest relates back to the time of filing the financing statement.[59] It is significant that, under the Uniform Commercial Code, a security interest may be perfected as against a subsequent judgment lien prior to the time such security interest becomes choate.[60]

Indeed, it appears that the interests specifically protected by sections 6323(c) and (d) would by necessity be inchoate at the time of tax lien filing. Section 6323(h)(1)[61] provides that a

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necessarily check the records. However, filing is of evidentiary value in determining the time at which the private interest arose. Furthermore, in cases where the competing interest is based on voluntary advancements within the forty-five day protection period, the government may desire to give actual notice to the competing lienor and thereby prevent the taxpayer from continuing to transform his property into cash. It is then essential that the government be able to determine the identity of the lienor, and this is facilitated by the filing requirement.

55. *Hearings on H.R. 11256 and H.R. 11290, supra* note 51, at 37.

56. UNIFORM COMMERCIAL CODE § 9-303. However, certain types of security interests may be perfected without the filing of a financing statement. *See* UNIFORM COMMERCIAL CODE § 9-302.

57. UNIFORM COMMERCIAL CODE § 9-204.

58. UNIFORM COMMERCIAL CODE § 9-303(1).

59. UNIFORM COMMERCIAL CODE § 9-312(5)(a); William Iselin & Co. v. Burgess & Leigh Ltd., 52 Misc. 2d 821, 276 N.Y.S.2d 659 (Sup. Ct. 1967).

60. Obligations covered by a security agreement may include future advances whether or not the advances are given pursuant to commitment. UNIFORM COMMERCIAL CODE § 9-204(5). In such a case the lien is inchoate because the amount of the lien is not fixed and definite. A security agreement may also provide that collateral, whenever acquired, shall secure all obligations. UNIFORM COMMERCIAL CODE § 9-204 (3). Thus, the property subject to the lien may be varied and, accordingly, it is not fixed and definite.

61. INT. REV. CODE of 1954, § 6323(h)(1) provides as follows:

The term "security interest" means any interest in property

security interest comes into existence when the debtor obtains the secured property and a disbursement is made by the secured party. Sections 6323(c) and (d) include only those transactions in which either the identity and extent of the property subject to the security interest will not be known or the amount of the secured claim will not be fixed and definite. Thus, by definition the interests protected by sections 6323(c) and (d) come into existence and become choate subsequent to the time the tax lien is filed.[62] The apparent purpose of sections 6323(c) and (d) is to preclude application of the choateness standards to those interests which come within the protected categories. The legislative history of the 1966 Act indicates that Congress so intended.[63]

Furthermore, by conditioning priority upon a finding that the secured party is protected under local law against a hypothetical judgment lien arising at the exact time the tax lien is filed, the rights of the federal government are equated with those of a local judgment lien creditor. Priority over the federal government is thus dependent upon perfection of the competing interest under local law. To the extent that the choateness doctrine may be inconsistent with the local priority system,[64] incorporation of the local system implicitly precludes application of the choateness doctrine.

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acquired by contract for the purpose of securing payment or performance of an obligation or indemnifying against loss or liability. A security interest exists at any time (A) if, at such time, the property is in existence and the interest has become protected under local law against a subsequent judgment lien arising out of an unsecured obligation, and (B) to the extent that, at such time, the holder has parted with money or money's worth.

62. *Cf.*, United States v. Ball Constr. Co., 355 U.S. 587 (1958), *reversing* 239 F.2d 384 (5th Cir. 1957), *affirming* 140 F. Supp. 60 (W.D. Tex. 1956).

63. Various types of secured creditor interests . . . are specifically defined, and . . . where those interests qualify under the definitions they are to be accorded this priority status whether or not they are in all other respects definite and complete at the time notice of the tax lien is filed.

112 CONG. REC. 25,420 (daily ed. Oct. 13, 1966). *See Hearings on H.R. 11256 and H.R. 11290, supra* note 51, at 38.

Similarly, in a government memorandum from the Commissioner of Internal Revenue, it was stated, "The bill attempts to solve these problems by providing specific exceptions to the choate test in new subsections (f) and (g) of section 6323." *Hearings on H.R. 11256 and H.R. 11290, supra* note 51, at 45. The memorandum was referring to an earlier draft of H.R. 11256. Subsections (f) and (g) of that draft dealt with future advances, obligatory advances, and certain financing agreements now covered by §§ 6323(c) and (d).

64. *See* text accompanying notes 27-29 *supra.*

C. THE NOTICE-FILING INTERESTS

The third change relevant to the choateness doctrine is the amendment to the notice-filing section. Section 6323(a), the notice-filing provision of the 1966 Federal Tax Lien Act, provides:

> The lien imposed by section 6321 shall not be valid as against any purchaser, holder of a security interest, mechanic's lienor, or judgment lien creditor until notice thereof . . . has been filed. . . .[65]

Arguably, the literal language of 6323(a) dictates that the interests specified should take priority over a tax lien at least until the tax lien is filed. However, the prior tax lien act included a substantially identical notice-filing section[66] which the courts refused to apply literally and denied priority to interests unless they were choate at the time the tax lien was filed.[67]

It is not clear whether Congress intended the 1966 Act to preclude application of the choateness doctrine to the notice-filing interests, thereby permitting a literal interpretation. The primary purpose in amending the notice-filing provision was apparently to include mechanic's lienors and to resolve previously existing terminology disputes.[68] The legislative history of the Act does not conclusively indicate that the purpose of section 6323(a) is to limit the choateness doctrine.[69] Conceivably, when Congress manifested its general intention to retain the choateness

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65. INT. REV. CODE of 1954, § 6323(a).

66. "[T]he lien imposed by section 6321 *shall not be valid* as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed. . . ." 68A Stat. 779 (1954) (emphasis added).

67. *See, e.g.*, United States v. Pioneer Am. Ins. Co., 374 U.S. 84 (1963); United States v. Ball Constr. Co., 355 U.S. 587 (1958).

68. *See Hearings on H.R. 11256 and H.R. 11290*, *supra* note 51, at 37, 49; H.R. REP. No. 1884, *supra* note 38, at 11, 36.

69. For example, the House Report states that

> Under decisions of the Supreme Court a mortgagee, pledgee, or judgment creditor is protected at the time notice of the tax lien is filed if the identity of the lienor, the property subject to the lien, and the amount of the lien are all established at such time . . . [S]ubsection (a) of new section 6323 retains this basic rule of Federal law . . . .

The Report then goes on to state that "the holder of a security interest has priority over a Federal tax lien if, at the time notice of the tax lien is filed, the security interest exists within the meaning of section 6323 (h) (1)." H.R. REP. No. 1884, *supra* note 38, at 35. Whether the definition of an existing security interest is subject to the choateness doctrine is not expressly resolved. *Compare* H.R. REP. No. 1884, *supra* note 38, at 2, 4; 112 CONG. REC. 25,420 (daily ed. Oct. 13, 1966); 112 CONG. REC. 21,293, 21,309 (daily ed. Sept. 1, 1966).

doctrine under the 1966 Act,[70] it at least intended that the doctrine should not be limited by the notice-filing provision. It is submitted, however, that in view of the nature of the interests included within the provision and the policy implicit in this and other related sections of the 1966 Act, the choateness doctrine should not be judicially applied to section 6323(a).

The interest of the mechanic's lienor was first added to the notice-filing provisions by the 1966 Act. This interest, as specifically defined in the Act,[71] is given protection as of the earliest date that such a lien would become valid under local law but not before the time at which the lienor commenced his services or furnished his materials.[72] The potential mechanic's lienor can thus be confident that the value he adds to the property will not be appropriated to pay the debts of the owner, provided he checks the records for a filed tax lien on the day to which his future mechanic's lien will relate back.

A result of the relation back privilege is to preclude subordination of the mechanic's lien to the federal tax lien by the application of the choateness doctrine. Even if the mechanic's lienor is required to comply with the choateness doctrine by reducing his lien to judgment, he may do so after the tax lien has been filed and the choate claim will relate back to the date previously set by local law. Thus, the critical factor in determining priority against a tax lien is the relation back date. Since the choateness doctrine does not alter this priority, the doctrine is abrogated with respect to a mechanic's lien.[73]

The notice-filing provision of the former tax lien act granted a judgment creditor priority over a subsequently filed tax lien. However, the interest of a judgment creditor was deemed inchoate by the courts unless the creditor also obtained a lien against specific property,[74] thereby making the property subject to the claim more certain and definite. Thus, the term "judgment

70. *See* note 42 *supra.*

71. INT. REV. CODE of 1954, § 6323(h)(2) provides in part:
The term "mechanic's lienor" means any person who under local law has a lien on real property . . . for services, labor, or materials furnished in connection with the construction or improvement of such property.

72. INT. REV. CODE of 1954, § 6323(h)(2).

73. Compare this to the superpriority interests of § 6323(b), which will prevail against the tax lien regardless of the time they become choate.

74. *See, e.g.*, Fore v. United States, 339 F.2d 70 (5th Cir. 1964), *cert. denied*, 381 U.S. 912 (1965); Ersa, Inc. v. Dudley, 234 F.2d 178 (3rd Cir. 1956); Beeghly v. Wilson, 152 F. Supp. 726 (N.D. Iowa 1957). *Cf.* United States v. Security Trust & Savings Bank, 340 U.S. 47 (1950).

creditor" was judicially rewritten to denote a "judgment lien creditor."

The 1966 Federal Tax Lien Act incorporated the term "judgment lien creditor" into section 6323(a). Arguably, Congress by adopting this term, approved application of the choateness doctrine to this extent.

Perhaps the most significant new term added to the 1966 notice-filing provision is "holder of a security interest." Under the prior act the terms "mortgagee" and "pledgee" were used. The substitution of "holder of a security interest," which includes mortgagees and pledgees, was intended to replace the former terms with a more general term used in the Uniform Commercial Code.[75]

The term "security interest" is defined in section 6323(h)(1) to be an interest in property acquired by contract for the purpose of securing payment or performance of an obligation. The Uniform Commercial Code definition of a "security interest"[76] is closely analogous. The security interest is deemed to exist, under the Tax Lien Act, only after the secured property exists, the security interest is protected under local law against a judgment lien, and the secured party has made disbursements. Thus the requisites to the existence of a security interest under the Act are roughly parallel to the conditions precedent to the attachment and perfection of a security interest under the Uniform Commercial Code.[77]

Whether or not a "holder of a security interest" under section 6323(a) is also required to comply with the requisites of choateness is suggested by reference to sections 6323(c) and (d). As previously noted, the 1966 Act negates application of the choateness doctrine to interests within sections 6323(c) and (d). Yet the practical differences between an inchoate interest which would take priority under subsections (c) and (d) and an in-

75. *Hearings on H.R. 11256 and H.R. 11290, supra* note 51, at 3-4.

76. "'Security interest' means an interest in personal property or fixtures which secures payment or performance of an obligation." UNIFORM COMMERCIAL CODE § 1-201 (37).

77. A security interest is perfected and accordingly protected against a subsequently arising judgment lien when a financing statement has been filed if necessary and when the security interest has attached. UNIFORM COMMERCIAL CODE §§ 9-303, 9-302. *See* William Iselin & Co. v. Burgess & Leigh Ltd., 52 Misc. 2d 821, 276 N.Y.S.2d 659 (Sup. Ct. 1967). The security interest will attach when the secured property exists and when the secured party has made a disbursement. UNIFORM COMMERCIAL CODE § 9-204.
CIAL CODE § 9-204.

terest which would be inferior under subsection (a), if the choateness doctrine is applied, does not suggest such drastically different legal consequences.

Illustrative is the common financing agreement under which a commercial factor agrees to make future disbursements to a manufacturer secured by the inventory of the manufacturer. In such a situation, the relative timing of the initial disbursement and tax lien filing would seem fortuitous. Yet application of the choateness doctrine to section 6323(a) imposes dramatic differences. For example, if the initial disbursement is made after the tax lien is filed, and assuming the other qualifications are met,[78] the secured party would take priority under section 6323(c). However, if the initial disbursement is made prior to the tax lien filing, the rights of the commercial factor are based on section 6323(a)[79] and application of the choateness doctrine would prevent the factor from obtaining priority.[80] The anomoly of this situation is even more apparent in situations involving a real property construction agreement or an obligatory disbursements agreement within section 6323(c). In such cases the secured party has priority even though the disbursements are made subsequent to tax lien filing and with actual knowledge of the filed tax lien. However, if disbursements are made prior to filing and without knowledge of the secret tax lien, the tax lien takes priority if the choateness doctrine applies.

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78. Specifically, the commercial factor must have filed a financing statement before the tax lien was filed, UNIFORM COMMERCIAL CODE §§ 9-303, 9-302, and the manufacturer must have rights in the secured property, UNIFORM COMMERCIAL CODE § 9-204. Note that under the 1966 Tax Lien Act the property securing a commercial transaction financing agreement may also include after acquired property. INT. REV. CODE of 1954, § 6323(c)(2)(B). *Compare* UNIFORM COMMERCIAL CODE § 9-204(3).

79. Assuming that the same qualifications specified in note 78 *supra* are met, the security interest will come into existence at the time of the first disbursement. *See* INT. REV. CODE of 1954, §§ 6323(h)(1)(A), (B). Since the initial disbursement is made prior to tax lien filing, §§ 6323(c) and (d), which only grant priority protection to those interests which come into existence after tax lien filing, is inapplicable. Section 6323(a), on the other hand, applies to security interests existing before tax lien filing.

80. Since the agreement contemplates further disbursements after tax lien filing, the amount of the secured party's claim is neither fixed nor definite and, accordingly, it is inchoate by federal standards. *See* United States v. Pioneer Am. Ins. Co., 374 U.S. 84 (1963); Crest Fin. Co. v. United States, 368 U.S. 347 (1961); United States v. Ball Constr. Co., 355 U.S. 587 (1958).

No justification exists for this harsh distinction favoring disbursements made after tax lien filing. Indeed, the policy of sections 6323(c) and (d) of the 1966 Act is that certain commercial transactions entailing a protected security interest and subsequent disbursements should be afforded priority over the tax lien. Application of the choateness standards to a substantially similar holder of a security interest seeking priority under section 6323(a) would frustrate the policy implicit in sections 6323(c) and (d).

Arguably, by negating the application of choateness to transactions covered by sections 6323(c) and (d) Congress merely singled out commercial financing agreements for special protection and no analogy can be drawn between these interests and interests included within section 6323(a).[81] However, it appears that Congress intended these sections to be construed in *pari materia*.[82] If the commercial financing agreements are not subject to the requisites of choateness, certainly the notice-filing interests should be similarly protected. It is not logical that certain security interests which, by their very nature, are incomplete at the critical time should receive greater priority against the tax lien than similar security interests which are complete.[83]

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81. Congress noted that the §§ 6323(c) and (d) interests are protected because they entail transactions expected to enhance the value of the property or because the secured party is obligated to make disbursements after the filing of the tax lien. 112 CONG. REC. 21,293 (daily ed. Sept. 12, 1966). However, the commercial financing agreements given priority under §§ 6323(c)(2), (4) and (d) do not necessarily enhance the value of the taxpayer's property any more than a security interest or the work resulting in a mechanic's lien under § 6323(a). Furthermore, the interests defined in §§ 6323(c)(2) and (3) and § 6323(d) generally do not obligate the secured party to make disbursements after the tax lien has been filed. Thus, the combined effect of these two rationales does not justify favored treatment for these specified interests to the exclusion of the notice-filing interests.

82. The House Hearings note that advances made under financing agreements secured by commercial financing security will be deemed to have priority if they arise within forty-five days after tax lien filing. It then goes on to state that "if notice has not been filed they will, of course, be protected as security interests against the unfiled Federal lien." *Hearings on H.R. 11256 and H.R. 11290, supra* note 51, at 38.

83. An interest is deemed a "security interest" within the protection of § 6323(a) only if the secured property is in existence at the time of tax lien filing and then only to the extent that the secured party has parted with money or money's worth. INT. REV. CODE of 1954, § 6323(h)(1). The interests protected by §§ 6323(c) and (d), on the other hand, include agreements in which either the secured property may not exist at the time of tax lien filing or the secured party has not parted with money or money's worth.

Furthermore, the policy of protecting reliance creditors against secret liens, which was the very basis for adoption of the former notice-filing provision, would similarly be frustrated. If the choateness doctrine is applied, the secured party under section 6323(a) would be inferior to a tax lien unless he either completed his performance under the contract or made the obligation fixed and ascertainable by the time the tax lien was filed. Because it is unlikely that he will be informed of the tax lien until notice thereof is filed, and since his obligation must be final at that time, the notice given by the filing would not provide the intended protection.[84]

The only notice-filing term retained unaltered by section 6323(a) is that of a "purchaser." Of significance is the fact that under the former act courts seemingly did not attempt to determine whether or not a purchaser's interest was choate. Rather emphasis was placed on the Treasury Regulation's definition of a purchaser,[85] and if an interest was deemed to be within this definition when the tax lien was filed it took priority over the lien. Thus, a competing purchaser was held to prevail against the federal lien where, at a time prior to tax lien filing, he acquired property or an interest in property[86] for consideration[87] that was both present[88] and valuable.[89]

There is no indication that Congress intended to abolish

84. It should be noted that the priority accorded disbursements made after tax lien filing as part of an agreement which also involved disbursements made prior to lien filing is not clearly resolved by the 1966 act. It is arguable that any advances after filing would not receive protection. Even assuming that the choateness doctrine were not applicable to § 6323(a), that section only grants priority to the extent that the secured party has actually made disbursements at the time the tax lien is filed. *See* INT. REV. CODE of 1954, § 6323(h)(1)(B). It seemingly does not grant priority for subsequent disbursements. Sections 6323(c) and (d) grant priority only to those security interests which come into existence after tax lien filing. Since a security interest comes into existence when both the secured property exists and disbursements have been made, *see* INT. REV. CODE of 1954 §§ 6323(h)(1)(A) and (B), the security interest will exist prior to filing. Consequently, the claim based on the subsequent disbursements is not within the literal construction of §§ 6323(a), (c) or (d) and may not be protected.

85. "The term 'purchaser' means a person who, for a valuable present consideration, acquires property or an interest in property." Treas. Reg. § 301.6323-1(a)(2)(a) (1954).

86. *See* United States v. Boston & Berlin Trans. Co., 188 F. Supp. 304 (D.N.H. 1960).

87. *See* United States v. Hoper, 242 F.2d 468 (7th Cir. 1957).

88. National Ref. Co. v. United States, 160 F.2d 951 (8th Cir. 1947); *See* United States v. Franklin Fed. Sav. & Loan Ass'n, 140 F. Supp. 286 (M.D. Penn. 1956).

89. Enochs v. Smith, 359 F.2d 924 (5th Cir. 1966).

this approach to the determination of a purchaser's priority. On the contrary, in view of the general policy of the Act to limit rather than expand the choateness doctrine,[90] and as the elements of this former definition of purchaser were incorporated into the 1966 Act,[91] the apparent intent of Congress was to grant protection to those interests coming within the definition of the term "purchaser" prior to the time of tax lien filing, without reference to the degree of choateness.

In general, the priority granted by section 6323(a) to a mechanic's lienor, a holder of a security interest, and a purchaser, like that granted to the section 6323(c) and (d) interests, is premised on the existence of protection under local law against certain hypothetical competing interests existing at the time of tax lien filing.[92] The effect of this incorporation of local law is to preclude application by the courts of a conflicting system such as that created by the choateness doctrine. Thus, future application of this doctrine to section 6323(a) would be inconsistent with the provisions and policy of the Tax Lien Act.

It is therefore concluded that when a private creditor of a delinquent taxpayer has an interest protected by section 6323, subsection (a), (b), (c), or (d) of the 1966 Federal Tax Lien Act, the relative priority between this interest and the tax lien should not be determined by application of the choateness doctrine. Rather, it is submitted that Congress substituted a definitional approach. If an interest qualifies within the definition of an interest protected by subsection (a), (b), (c), or (d) of section 6323, it is to be afforded the priority status granted by the respective subsection whether or not it is in all other respects choate at the time the tax lien is filed.[93]

90. *See Hearings on H.R. 11256 and H.R. 11290, supra* note 51, at 64.

91. "The term 'purchaser' means a person who, for adequate and full consideration in money or money's worth, acquires an interest . . . in property which is valid under local law against subsequent purchasers without actual notice." INT. REV. CODE of 1954, § 6323(h)(6).

92. The significant factor in determining the priority afforded a mechanic's lienor against any competing interest is the relation back privilege which, under the new Act, is determined by local law. INT. REV. CODE of 1954, § 6323(h)(2). Similarly, a security interest is by definition one that under local law will prevail against a subsequent judgment lien. INT. REV. CODE of 1954, § 6323(h)(1). Finally, the 1966 Tax Lien Act adopts the definition of purchaser contained in Treas. Reg. § 301.6323-1(a)(2)(a), but adds that the interest must be valid under local law against subsequent purchasers without notice. INT. REV. CODE of 1954, § 6323(h)(6).

93. *See* H.R. REP. No. 1884, 89th Cong., 2d Sess. 2 (1966); 112 CONG. REC. 25,420 (daily ed. Oct. 13, 1966). Once this priority has been established it may also extend to the costs and expenses of preserving the

IV. CONSEQUENCES OF LIMITING THE CHOATENESS DOCTRINE

A. Impact Upon Federal Tax Collection

Although the choateness doctrine often worked injustice upon third parties, it nevertheless served a useful and important purpose. Taxes are a necessity of government, and their prompt and certain availability is an imperious need.[94] The tax lien, which is an exercise of Congress' constitutional power "to lay and collect taxes,"[95] is essential to the fulfillment of this governmental need. Consequently, private and local interests should not be permitted to undermine the exercise of this power by means of competing liens which are uncertain in amount and which attach at an indefinite or arbitrary time to unascertained property.[96]

The 1966 Act, while modifying the choateness doctrine, does not abandon the policy which motivated its development. The 1966 Act does not permit vague and contingent interests to undermine and frustrate tax collection. All interests included within the priority definitions are characterized by a high degree of specificity and perfection.

For example, purchasers, by definition, have an interest in specific property and the amount of this interest can be absolutely determined by the consideration paid therefor. A holder of a security interest has a priority right only if the secured property exists and only to the extent that he has parted with money or money's worth. Thus, at the time of the tax lien filing the property subject to the secured party's lien and the amount of that lien is definitely ascertainable. The property

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security interest if local law gives such item the same priority as the lien or security interest to which it relates. Int. Rev. Code of 1954, § 6323(e).

94. Bull v. United States, 295 U.S. 247, 259-60 (1935).

95. U.S. Const. art. I, § 8. *See* Michigan v. United States, 317 U.S. 338 (1943); United States v. White Bear Brewing Co., 227 F.2d 359 (7th Cir. 1955).

96. *See* United States v. City of New Britain, 347 U.S. 81, 86 (1954), where the Court suggested that potential impairment of federal standing may have been the motivating factor behind the development of the general and unperfected lien doctrine.

Without some limitation, a situation could arise in which a lender is able to loan money indiscriminately to a taxpayer long after a tax lien is filed and thereby give those advances the priority of an earlier mortgage. "The choate requirement has thus served a useful and important purpose and would be retained by the bill." *Hearings on H.R. 11256 and H.R. 11290, supra* note 51, at 47.

subject to a mechanic's lien is likewise known, and the amount of the lien can thereafter be determined by calculation or by reducing it to a judgment.[97] Moreover, all judgment lien creditors by definition meet the requisites of choateness.

The priority claims of creditors competing with the federal government under section 6323(c) extend only to specific, "qualified property" determined by a contractual agreement and limited by the Act. Protection under section 6323(d) extends only to secured property previously designated and in existence at the time the tax lien is filed. Furthermore, the protected disbursements made pursuant to section 6323(c)(2) or (d) must be made within a restricted time period.

Finally, most interests given priority are required to be protected under local law against judgment creditors. Thus, to prevail against the tax lien the competing interest must be sufficiently fixed and definite to prevail against other local creditors.[98]

B. Impact Upon the Circuity of Lien Rights Problem

The doctrine of choateness formerly permitted courts to determine the relative priority of interests competing with the federal tax lien without regard to state or local priority rules. Exclusion of the choateness doctrine from the interests specifically defined in the 1966 Act, while also requiring the interests to possess a priority status under local law, has brought the priority system into accord with the state rules of priority.[99]

97. It should also be noted that a limited superpriority is given to mechanic's liens for certain repairs and improvements of residential property not in excess of $1000. Int. Rev. Code of 1954, § 6323(b)(7). This eliminates the necessity searching for filed tax liens prior to undertaking small repair projects for home owners.

98. The significance of this requirement is evidenced by application of the 1966 tax lien act to the facts of United States v. Ball Constr. Co., 355 U.S. 587 (1958). It has been contended that the *Ball* decision, which was likely a prime force behind adoption of § 6323(c), would be reversed in favor of the surety under that section. Creedon, *The Federal Tax Lien Act of 1966*, 20 A.B.A. Sect. Tax. Bull. 101, 121-22 (1967). However, the interest of the surety had not been perfected under local law against competing creditors, *see* R. F. Ball Constr. Co. v. Jacobs, 140 F. Supp. 60 (W.D. Tex. 1956); Note, 43 Minn. L. Rev. 755, 767 (1959), and therefore the *Ball* decision would likely remain unchanged.

99. The Supreme Court has stated that it would be contrary to the federal policy of uniformity in federal tax laws to permit the diverse rules of various states to determine relative priority of federal tax liens. United States v. Equitable Life Assurance Soc'y of the United States, 384 U.S. 323, 331 (1966); United States v. Speers, 382 U.S. 266, 270 (1965). However, this alleged diversity is minimized by adoption of the Uniform Commercial Code in nearly every state.

The result is a substantial elimination of the conflicting two-priority system. Accordingly, the major circuity of lien rights problem is alleviated.

Specifically, the 1966 Federal Tax Lien Act affords the same protection to mechanic's liens against unfiled tax liens as that given to competing security interests.[100] Thus, in the circuity situation discussed earlier,[101] the mechanic's lien for services commenced before the mortgage is perfected will take priority over the mortgage which, in turn, will take priority over a subsequently filed tax lien.[102]

C. INTERESTS REMAINING SUBJECT TO THE CHOATENESS DOCTRINE

Under the 1966 Tax Lien Act, the choateness doctrine will be applied to those interests not specifically included within section 6323. Thus, attachment liens,[103] garnishment liens,[104] and

100. Similarly the act provides superpriority status to those state real property tax liens which are granted preferential treatment under local law against competing interests. The combined effect of these two provisions is to completely eliminate the circuity of lien rights problem that existed in United States v. City of New Britain, 347 U.S. 81 (1954).

101. *See* text accompanying note 31 *supra*.

102. Parenthetically, it should be noted that a limited circuity of lien rights problem may still arise under the provisions of the 1966 Act. INT. REV. CODE of 1954, § 6323(h)(2) permits a mechanic's lien to relate back to the date that work was commenced or supplies furnished. However, some state laws give the mechanic's lien a relation back to an earlier time. If a mortgage is perfected during the period between the different dates to which relation back is permitted, state law may give the mechanic's lien a priority over the mortgage whereas the federal law will not because the mortgage arose before the date of relation back permitted by § 6323(h)(2). Furthermore, if the tax lien were filed after the mortgage was perfected but before the date to which the mechanic's lien relates back under § 6323(h)(2), the mortgage but not the mechanic's lien would be superior to the tax lien whereas local law would give the mechanic's lien priority over the mortgage. The result is a circuity of lien rights.

If a circuity problem does arise, it likely will be resolved in a manner similar to that articulated in the *New Britain* decision. United States v. City of New Britain, 347 U.S. 81 (1954). *See* United States v. Buffalo Sav. Bank, 371 U.S. 228 (1963), where the Supreme Court reversed per curiam because of the failure of the lower court to apply the *New Britain* resolution to a circuity problem.

The American Bar Association recognized that the *New Britain* rule was not completely equitable, but was preferable to any possible alternative. Consequently, it recommended that the rule be confirmed by statute. *Hearings on H.R. 11256 and H.R. 11290, supra* note 51, at 108. The 1966 Act, however, makes no reference to the *New Britain* resolution.

103. *See* United States v. Acri, 348 U.S. 211 (1955); United States v. Security Trust, 340 U.S. 47 (1950).

104. *See* United States v. Liverpool & London Ins. Co., 348 U.S. 215 (1955).

landlord's distress liens[105] are still required to be choate and, because these interests are not included within the notice-filing provision, they must be choate before the tax deficiency is assessed. This does not seem unfair. These creditors generally have not advanced credit in reliance on the property subject to the tax lien. Therefore, they do not have the same equitable position against the government as that of contract lienors or of those who extend credit secured by specific property.

The possessor of an interest which remains subject to the choateness doctrine, however, may still prevail against the tax lien even though his competing interest is inchoate. Under the former act, a competing interest could prevail by a showing that the security was not property of the taxpayer to which the tax lien could attach.[106] The definition of property is a matter governed by state and local law, and the 1966 Tax Lien Act did not reflect in any way on the question of what constitutes property subject to the tax lien.[107]

V. CONCLUSION

The 1966 Federal Tax Lien Act appears to reach a reasonable accommodation between the interest of the federal government in collecting delinquent taxes and the right of taxpayers and third party creditors whose interests are affected. Moreover, it adjusts the tax lien provisions of the Internal Revenue Code to modern commercial practices.

Under the 1966 Act, the federal government will still take priority over competing interests that are not specifically defined and that are not definite and complete at the critical time. The interests which prevail against the federal government will either be choate and first in time to the tax lien, or they will be within the specific provisions of the Act, in which case the interests have attained a high degree of certainty and specificity. Although certain interests are given an absolute exemption from the tax lien, they are generally transactions involving relatively limited monetary amounts in situations in which it is unreasonable to require the parties to check records.

The creditor or commercial financier may now be assured that the substance of his disbursements as well as the security for these disbursements will not be confiscated by the federal

105. *See* United States v. Scovil, 348 U.S. 218 (1955).
106. *See* note 27 *supra.*
107. *Hearings on H.R. 11256 and H.R. 11290, supra* note 51, at 48; H.R. REP. No. 1884, *supra* note 93, at 11n.2.

government to pay the delinquent taxes of his debtor. The creditor may check for a filed tax lien and, if no lien is filed, he may thereafter enter a financing agreement with the taxpayer. By adopting an agreement that qualifies within the specific provisions of the 1966 Act, he can be confident that his secured property will not be subject to the tax lien.